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Trial Affidavit of Charles Hannaford

UNITED STATES DISTRICT COURT
DISTRICT OF MASSACHUSETTS

IN RE PHARMACEUTICAL INDUSTRY AVERAGE WHOLESALE PRICE LITIGATION	MDL No. 1456
THIS DOCUMENT RELATES TO: ALL CLASS ACTIONS	CIVIL ACTION: 01-CV-12257-PBS Judge Patti B. Saris

TRIAL AFFIDAVIT OF CHARLES HANNAFORD

I, Charles Hannaford, pursuant to 28 U.S.C. § 1746, on oath, depose and state as follows:

1. I am a resident of the Commonwealth of Massachusetts. I have personal knowledge of the facts stated below, would so testify in court if called upon to do so, and am competent to provide testimony.

2. I am the Fund Administrator for the Pipefitters Local 537 Trust Funds (the "Fund" or "Pipefitters"). I have been the Fund Administrator since March 1, 2003. I have been a member of the Pipefitters Local 537 Union (the "Union"), and have personally received benefits through the Fund as a member of the Union, continuously since approximately 1975. Pipefitters is a representative for Class 3.

3. As the Fund Administrator I run the day-to-day aspects of the Fund and advise the Board of Trustees regarding policy issues that arise during its administration. I am familiar with the operation of the Fund and specifically with the health benefits offered to members of the Union through the Fund and the Fund's payment for such benefits, including physician-administered drugs.

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4. My formal education consists of an undergraduate degree in Business from Boston University in 1966. I also obtained a Masters Degree in systems management from the University of Southern California in 1970.

5. After a four year apprenticeship ending in 1979 I worked full-time for Honeywell Controls in Newton, Massachusetts until approximately 1984. At that time I went to work for Carrier Air Conditioning in the Boston area and was employed by Carrier until 2002 with the exception of two time periods. In 1991, as a member of the Air Force Reserves I was activated into full-time service during Operation Desert Storm. I returned to Carrier Air in 1993. In addition, for two years beginning in 1987 I worked for Jaymont Management Company.

6. All of the Fund's operations are conducted from its location at 35 Travis Street, Unit One, Allston, Massachusetts. The Fund operates out of a small space of approximately 1,300 square feet. The staff of the Fund is likewise very small, consisting of myself and five other employees in total. The other employees consist of an office manager, one employee who deals primarily with qualified domestic relations orders, and three other employees who each only have individual responsibility for issues related either to pension benefits, annuity benefits, or the health and welfare benefits provided to Union members.

7. The Fund is a Taft-Hartley Fund, governed by a Board of Trustees consisting of three trustees appointed by management and three labor trustees. In addition to providing a number of other benefits, the Fund provides major medical benefits, including prescription drug benefits, to all union members and their eligible dependants.

8. Currently there are approximately 4600 individuals, both union members and their dependants, who receive major medical benefits, including prescription drug benefits, through the Fund.

9. Members of the Fund are tradesmen and tradeswomen who work on buildings systems, including but not limited to heating ventilation and air conditioning (HVAC) systems. Members of the Union and of the Fund generally work and live in Eastern Massachusetts in an area bounded north by Salem, Massachusetts, West by Interstate 495 and South by Route 128 in Massachusetts.

10. The Fund finances medical and other benefits for its members through employer contributions negotiated by the Union through the collective bargaining process. The Fund is self insured. The Fund is fully responsible and at-risk for all payments made for medical benefits, including pharmaceutical products, administered to its eligible members, within the parameters of the coverage provided by the Fund and outlined for its members in the summary of benefits. In general, the Fund covers 90% of all costs associated with treatment of its members, including the cost of pharmaceuticals.

11. Since approximately 1979 the Fund has contracted with Blue Cross/Blue Shield of Massachusetts ("BCBSMA") to administer the major medical benefit, including coverage for all prescription benefits, provided to members. The financial arrangement between the Fund and BCBSMA is "cost plus" meaning that BCBSMA charges the Fund whatever it pays for the particular service or pharmaceutical plus an administrative fee. In this way the Fund is fully responsible for all costs associated with benefits provided to its members.

12. Based on the claims data obtained through BCBSMA, the Fund has paid for the following drugs made by the following defendants:

Track I Defendant	Drug Reimbursed by Pipefitters
AstraZeneca	Zoladex
Bristol Myers Squibb	Blenoxane Cytoxan Etopophos Paraplatin Rubex Taxol Vepesid
Johnson & Johnson	Procrit Remicade

13. Until beginning my position as Fund Administrator I had not encountered the term "AWP" or Average Wholesale Price. When I began as Fund Administrator I was told by staff who had been working at the Fund for approximately twenty years that the AWP was in fact the average wholesale cost of a particular drug. At the time Pipefitters had a small program for retirees through a PBM and had contracted to provide very limited prescription coverage to retirees of up to $700 per year. That contracted reimbursement paid by the Fund under that program for brand name drugs was AWP less 18%. The Fund subscribed to the RedBook in order to spot check the prices being paid to ensure that the Fund was being charged 18% less than the published average wholesale price. I believed that the published AWP was in fact the actual average of wholesale prices for the drug.

14. It was not until approximately March 31, 2003 when I read an article in the *Wall Street Journal* Entitled "Hired to Cut Costs, Firms Find Profits in Generic Drugs," attached hereto as Exhibit A, that I or members of the Fund staff came to understand that the published AWPs were not the actual average of wholesale prices. Shortly thereafter I brought this article and the subject matter of AWP inflation to the attention of my staff and to members of the Board of Trustees. This was the first time any of them had any indication that the published AWPs were not in fact the average of wholesale prices.

15. Although the *Wall Street Journal* Article attached as Exhibit A concerns the discounts off of AWP available to PBMs it does not identify the drugs which are subject to such discounts and does not discuss the role Defendants in this litigation play in setting the AWP or in marketing the difference between their published AWP and the actual acquisition cost to providers as a means of selling more of their products. No one at the Fund has ever had any communications with any drugs companies concerning the relationship between AWP and the actual prices at which their drugs are available for purchase by providers.

16. None of the drug companies have sent me or the Fund to my knowledge information concerning the spread between AWP and acquisition cost.

17. None of the drug companies have sent me or the fund to my knowledge any of their marketing material sent to doctors which discuss the spread between AWP and acquisition cost.

18. At some point in late 2004 I also became aware that through its contract with BCBSMA, the Fund was also paying for certain pharmaceuticals at a price that is based on the published AWP. The particular prices paid by the Fund for medical services and pharmaceuticals are not separately negotiated by the Fund. The Fund is much too small and has

too few resources to undertake such a task. The prices paid by the Fund are those paid by BCBSMA for the particular drug or service and I understand from my attorneys that individuals at BCBSMA have testified under oath that they reimburse physicians for physician administered drugs at issue in this case at 95% of the AWP.

19. I first heard of this litigation involving AWP at a meeting of the Massachusetts Coalition of Taft-Hartley Funds sometime in the summer of 2005. This coalition is a group of funds very similar to the Fund whose administrators meet periodically to discuss issues relevant to health care, pension and annuity benefits provided to their members. It consists of approximately 15 Taft-Hartley funds, all of whom, like the Fund, contract with larger entities to administer their health benefits. In my experience many, if not the vast majority, of the Taft-Hartley funds of which I am aware through the Massachusetts Coalition contract with BCBSMA in much the same way the Fund does for administration of their benefits.

20. Despite my awareness of the *Wall Street Journal* article in March 2003, I still had insufficient information at that time to determine whether the AWPs were inflated over the actual prices being paid by health care providers for these drugs and if inflated, how much that inflation was. The Fund lacks the resources in both time and money to undertake such a wide ranging and in-depth analysis. Until approached about participation in this lawsuit in the summer of 2005, I feel I did not possess sufficient knowledge or information concerning the nature or extent of the AWP inflation to bring suit. To the best of my knowledge, the Fund could not have discovered the AWP scheme outlined in the complaint in this matter any sooner than it did.

21. Although the Pipefitters fund may not have focused on AWP at the time it was paying drug benefits, we did expect that whatever was the basis for calculating our prescription costs would be calculated on a fair basis and that our prices and pricing benchmark would not be

subject to manipulation. We did not expect drug companies to use the government's Medicare AWP based payment scheme as a means to market the spread to doctors, resulting in inflated pricing benchmarks in the industry and that this manipulation would impact our fund as AWP is also the pricing benchmark in the non-Medicare sector.

22. I also understand that defendants claim that BCBSMA was aware of the AWP Scheme alleged in this litigation and that as our "agent" agreed to pay inflated prices with our authorization. We have not authorized BCBSMA to agree to pay inflated prices for drugs on our behalf.

23. I make the foregoing statements under penalty of perjury on the date written next to my name below.

Date: October 27, 2006

Charles Hannaford

EXHIBIT A

Case 1:01-cv-12257-PBS Document 3049 Filed 08/31/2006 Page 2 of 6

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DOWJONES

Rx for Margins

Hired to Cut Costs, Firms Find Profits In Generic Drugs

Pharmacy-Benefit Managers Can Take Huge Markups And Still Offer 'Discounts'

Making $170 on Just 90 Pills

By BARBARA MARTINEZ

Pharmacy-benefit managers, the companies behind the cards most Americans use to fill prescriptions, promise to cut costs for employers and health plans. But they have found a way to squeeze impressive profits in an unlikely place: generic drugs.

Express Scripts Inc., one of the four big players that dominate this middleman business, made a $170 profit last summer on a single 90-pill prescription for the generic version of Prozac, according to billing documents. The antidepressant was purchased by a retiree from Terex Corp., a Westport, Conn., construction-equipment manufacturer.

In another instance, Express Scripts pocketed up to $18 on smaller 60-pill prescriptions for generic Prozac, or fluoxetine, bought last September by beneficiaries of Primary Health Inc. in Boise, Idaho. The state of Arkansas found last year that another major company in the business, AdvancePCS, had made profit margins averaging 22% for processing generic prescriptions for public employees.

Pharmacy-benefit managers, or PBMs, say their mass buying power allows them to obtain discount prices for employers and health plans. PBMs also steer doctors to less expensive generics. Express Scripts says it goes so far as to take losses on "a significant number" of brand-name prescriptions. "There is no other part of the supply chain that is trying to make drugs more affordable," says Barrett Toan, the company's chief executive.

But even in a rocky economy, Express Scripts and its rivals are enjoying robust financial results. Ranked third in its industry based on the 50 million people it covers, St. Louis-based Express Scripts reported that its net income grew 63% last year, to $202.8 million. The company, in business since in 1986, has said it expects its earnings per share to grow by up to 25% this year. AdvancePCS, the nation's largest publicly traded PBM,

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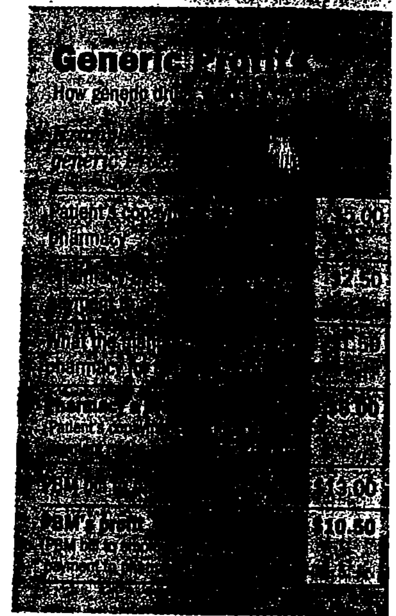
Case 1:01-cv-12257-PBS Document 3049 Filed 08/31/2006 Page 3 of 6



has said its earnings grew 44% for tl nine-month period that ended Dec. 3 compared with the year-earlier period.

Growth in prescription volume a counts for a lot of the industry's prospe ity. But there is another engine propellin PBM success: the surprising leeway thes companies have discovered to collect fa margins on some generic prescriptions.

Competing fiercely to sell look-alik products, generic manufacturers have li tle leverage on price. That means tha even after huge markups, generics ca seem inexpensive to clients.

Overall drug costs continue to rise re lentlessly, by more than 15% a year na tionwide. As employers search for an relief available—especially by shifting t generic drugs—just how much PBM

Please Turn to Page A6, Column 1

INDEX

A6 MONDAY, MARCH 31, 2003 THE WALL STREET JOURNAL.

Pharmacy-Benefit Firms Profit on Generic Drugs

Continued From First Page

make from generic prescriptions is an important question for employers and patients. Express Scripts says that close to half of the 300 million prescriptions it processes annually are for generics, and the proportion is growing.

In the complicated and at times counterintuitive world of drug pricing, many employers and health plans say they don't know what margins their PBM is collecting. Terex is a case in point. Beginning in the late 1990s, Express Scripts provided pharmacy benefits for about 100 Terex retirees. When one retired Terex employee ordered a 90-pill prescription for a generic version of the ulcer medication Zantac last July, Express Scripts paid the pharmacy $15, billing documents show. The bill to Terex was $215, meaning a $200 profit for the PBM.

Terex didn't have a clue about the markup. "You're kidding me," says Kevin Barr, the company's vice president of human resources, when told of this and other transactions. "If that's happening, that's pretty infuriating." (The Wall Street Journal reviewed pharmacy billing statements generally not available to client companies.)

Express Scripts says that focusing on its profits from generics is unfair, since such gains are balanced out by losses on some brand-name prescription medicines. Overall, the PBM says it saves clients huge sums.

Express Scripts says it "fully discloses" to clients such as Terex that it may keep the difference between what the client pays and what the pharmacist receives. The huge margins on the Terex transactions "resulted from an out-of-date contract that no longer applies to any of our clients," the company said in a written statement. The PBM adds: "Only a tiny number of contracts representing just one-tenth of 1% of our members were still affected by this situation in 2002." Terex didn't sign a new contract with Express Scripts when the old one expired in December 2002.

One reason that some employers and health plans may assume they are saving more than they really are on generics is PBMs' focus on "average wholesale prices," or AWPs. These prices for drugs are collected and published by industry trade magazines and data bases. PBMs often market themselves based on large discounts from AWPs that they offer clients—sometimes as much as 60%.

'Ain't What's Paid'

But it's an open secret in the industry that AWPs often are severely inflated, says Robert Garis, a pharmacy professor at Creighton University in Omaha, Neb., who is studying pricing by PBMs. Some industry veterans joke that AWP ought to stand for "Ain't What's Paid." This is especially true in the generic market, where manufacturers routinely undercut the published AWPs.

The resulting discrepancies mean that discounts from AWPs often aren't as favorable as they sound. The typical AWP for fluoxetine is now about $2.66 a pill. With a 60% discount, that comes down to about $1.06 a pill. But pharmacies can buy the antidepressant for about five cents a pill. Allowing for a standard markup, a PBM may pay a pharmacist about 30 cents a pill for fluoxetine—still much less than the $1.06 a pill the PBM is collecting from the health plan.

Express Scripts says that currently its clients pay less than 60 cents a pill for fluoxetine. But even if its clients pay only 50 cents, in many cases Express Scripts would still be making a 100% profit margin. That's because it pays stores only 25 cents per pill or less, according to pharmacy price lists.

In October, Express Scripts put out a press release saying that by using fluoxetine, instead of Prozac, which is made by Eli Lilly & Co., its clients save an average of $53.82 per prescription. Yet for some clients, there would be even more room for savings if PBMs took less hefty profits.

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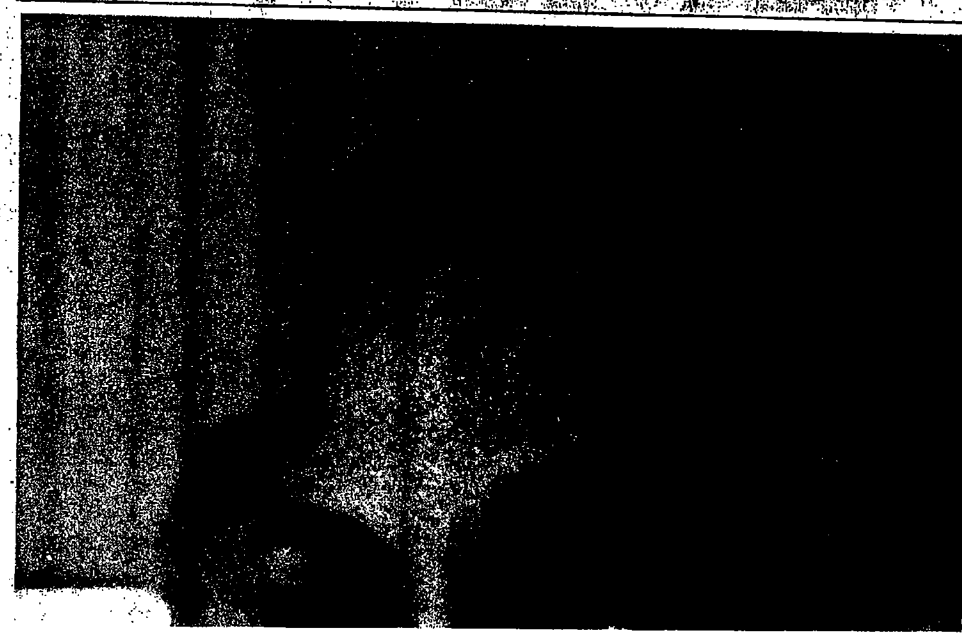

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THE WALL STREET JOURNAL.

: on Generic Drugs

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Primary Health, the Boise health plan, employs Express Scripts to provide drug benefits for its 13,000 members. Informed that the PBM has made profits of up to $18 on 60-pill fluoxetine prescriptions, Primary Health's chief executive, Elwood Kleaver, says he is surprised his company has paid such large margins for the nation's most commonly prescribed generic drug. "I'm upset about it," Mr. Kleaver says. "But I don't know that there's anything I can do about it."

Referring to the Primary Health example, "and the overall subject of your article," Express Scripts says that "any general numerical range can be inaccurately presented out of context." Generic drugs typically cost 80% less than comparable brands, the PBM says. That means that "when it comes to generics, our interests are fully aligned with those of our clients, members and retailers."

Traditionally, PBMs received only modest administrative fees for arranging prescriptions at cost. But they increasingly are reducing those fees and trying to take advantage of the "spread" between pharmacy prices and what corporate and government clients pay. Express Scripts says most of its contracts now include spread pricing.

Patients themselves are not immediately affected by PBM margins, since most people simply make a flat $5 or $10 copayment to the druggist. But employer and health-plan costs eventually trickle down, affecting premiums, benefit levels and copayments.

All told, Express Scripts says that its average net income per prescription—including both branded and generic drugs—is only 46 cents. Comparable figures at the other three major PBMs range from about 25 cents to $2.

Together, AdvancePCS, Express Scripts, Merck & Co.'s Medco unit and Caremark RX Inc. form the PBM oligopoly. They say they control the drug benefits of 210 million people in the U.S., or 70% of the nation's population.

Like Credit-Card Providers

Over the past decade, nearly every major U.S. employer has handed over the management of drug benefits to one of the four major PBMs. Like credit-card providers, PBMs made themselves essential by creating electronic networks that automated purchasing and billing. But many clients don't monitor their PBMs closely. Those that do so discover that PBMs refuse to reveal what they pay druggists. The PBMs call this information "proprietary and confidential."

The state of Arkansas hired AdvancePCS in 2000 to provide benefits to 135,000 state employees. The contract called for AdvancePCS to pass through pharmacy prices without any markup and receive administrative fees of 24 cents per claim, as well as a share of certain drug-manufacturer rebates. Instead, an auditing arm of the Arkansas legislature found last year that AdvancePCS, which provides benefits for 75 million people nationwide, was charging the state more for many prescriptions.

The audit agency found, for example, that in January 2002, AdvancePCS charged the state $18.39 for a generic prescription of the pain killer propoxy, having paid the pharmacy only $13.32, keeping $5.07 for a 38% profit. The audit report concluded that AdvancePCS overcharged the state a total of $479,000 on generic drugs over a four-month period.

AdvancePCS told auditors, according to the report, that a computer-programming error caused the overcharging. The company, which has paid back the disputed amount, says, it and Arkansas "are pleased with our relationship and the results that our partnership has generated for the client." Sharon Dickerson, the state's employee-benefits chief, says that overall, AdvancePCS helped Arkansas save about $4 million in 2002.

Some employers and health-plan administrators concede they don't have a handle on PBM profits. "The whole system is so convoluted and complicated," says Therese Hanna, Mississippi's insurance administrator, who oversees $70 million in drug spending for state employees and their relatives. She says she doesn't know what profits the state's PBM, AdvancePCS, makes on prescriptions. Asked for comment, AdvancePCS says in a written reply: "~~Our clients' competitive bidding process drives the rates and savings they~~"

Document 3049 Filed 08/31/2006 Page 6 of 6

drug spending for state employees and their relatives. She says she doesn't know what profits the state's PBM, AdvancePCS, makes on prescriptions. Asked for comment, AdvancePCS says in a written reply: "Our clients' competitive bidding process drives the rates and savings they can achieve through retail network discounts. We hold ourselves accountable to our clients for achieving these savings."

Large spreads often aren't available with branded drugs because there is less competition and therefore less undercutting of AWP. With manufacturers—and, in turn, pharmacies—setting actual prices closer to AWP, there is less of a potential margin for PBMs.

Even on those relatively rare occasions when a client audit forces a PBM to pay back some of the margin it has collected on generic prescriptions, there can be plenty of profit left over.

According to an audit made public last September, Express Scripts overcharged the New York state employees' prescription-drug plan, which covers 1.1 million people. The company charged New York AWP minus 14% for certain generic drugs, rather than the amount New York had contracted for: AWP minus 39%. The difference, involving some 37,000 claims over a 15-month period, resulted in New York making excess payments of about $613,000, according to a September 2002 letter from the state to Express Scripts.

In a written statement, the company attributed the overcharge to "human error, occasioned by a no-longer-used claims-adjudication system." The error affected only claims from out-of-state pharmacies that amounted to "less than 0.1%" of New York's total, the company said. On the "vast majority" of the state's claims, Express Scripts said it took no spread at all. The company said it repaid the overcharge and "took steps to ensure the error did not happen again."

But even at the promised discount of AWP minus 39%, Express Scripts probably makes out just fine. The company typically pays pharmacies much less than that. In the case of atenolol, a widely used blood-pressure medication, Express Scripts pays pharmacies the equivalent of about AWP minus 91%, according to pharmacy price lists. Asked about this comparison, the company says atenolol prescriptions weren't part of the New York audit.

Boots & Coots

Fighter of Oil-Well Fires in Iraq Rejects Voluntary Restructuring

A small Houston firm fighting oil-well fires in Iraq said it rejected a restructuring proposal from a creditor that would have required a voluntary Chapter 11 bankruptcy filing. But Jerry Winchester, chief executive of Boots & Coots International Well Control Inc., said its financial woes wouldn't affect its ability to fight more Iraqi oil-well fires. Boots & Coots said that it paid off the balance of a $1 million loan from Checkpoint Business Inc., a Panamanian-incorporated creditor that proposed restructuring because of the company's

"analytical in nature and were not intended to be anything more."

A Pulitzer-Prize winning journalist for his coverage of the Vietnam War when he worked for the Associated Press, Mr. Arnett rose to prominence during the first Gulf War, which he covered from Baghdad for CNN.

Third Infantry Division," with which was traveling. That report headlin Wolf Blitzer's summary in the late aft noon and Lou Dobbs Moneyline in t early evening. "It is not known at th point whether the Iraqis would attack t U.S. units here in a sandstorm and night, but that's a possibility and ever

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